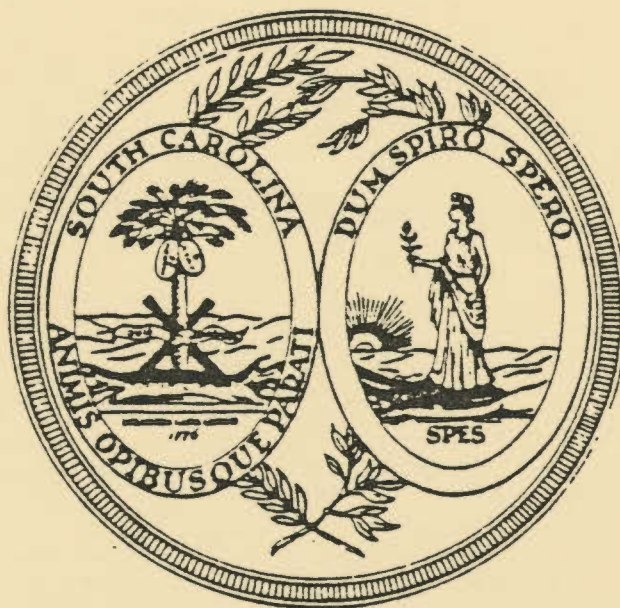


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STATE DOCUMENTS

South Carolina General Assembly



Legislative Audit Council



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The State of South Carolina
General Assembly
Legislative Audit Council
A Review of Legislative Oversight
in the State Budget Process
January 16, 1980

THE STATE OF SOUTH CAROLINA

GENERAL ASSEMBLY

LEGISLATIVE AUDIT COUNCIL

A REVIEW OF LEGISLATIVE OVERSIGHT

IN THE

STATE BUDGET PROCESS

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BACKGROUND

A budget system for the State of South Carolina was officially established in law by Act 130 of 1919. The Act provided that the Governor be chief budget officer of the State, and, as such, submit a budget to the General Assembly, based on his own conclusions and judgments, within five days after the beginning of each regular session. The first budget presented under this law was for the year 1920, and involved a total recommendation of \$5,466,632.

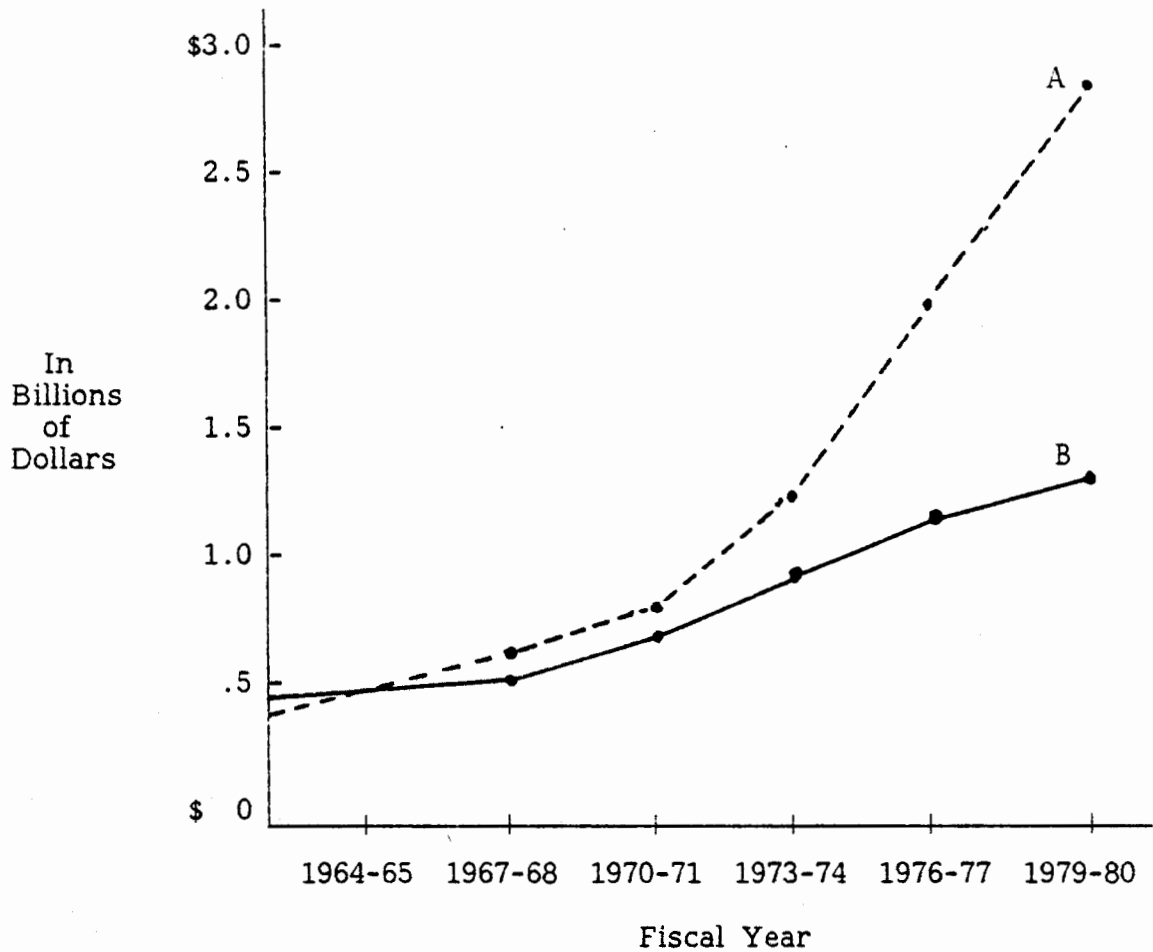
In 1933 a temporary provision was included in the Appropriation Act establishing a Budget Commission comprised of the Governor, Chairman of the House Ways and Means Committee and Chairman of the Senate Finance Committee. It became this Commission's responsibility to present the budget recommendation to the General Assembly. The first budget officially presented by the Budget Commission, for FY 32-33, encompassed \$6,502,240 of State funds.

The temporary provision establishing the Budget Commission was included in every Appropriation Act thereafter until Reorganization Plan Number 2 was enacted during the 1950 session of the General Assembly. This Plan established the Budget and Control Board, with the Governor as Chairman and the Comptroller-General, Treasurer, Chairman of the House Ways and Means Committee and Chairman of the Senate Finance Committee as its members. The first Budget and Control Board budget, submitted to the General Assembly for FY 51-52, included a total recommendation of \$83,794,925. The State's budget continues to be prepared by the Budget and Control Board. For FY 80-81 its total recommendation amounts to \$3,316,929,128 which includes State, Federal and other funds.

The Audit Council reviewed the growth of the budget figures as presented in the fund source analysis section of the State's budget documents for every third year since 1965. It was found that the total budget, expressed in constant 1965 dollars, has more than tripled since 1965. The average yearly rate of growth over this period was 27%. In FY 64-65 State funds accounted for 76% of the budget, and Federal funds 20%. In FY 79-80 State funds accounted for 60% of the budget, and Federal funds 30%.

GROWTH IN STATE AGENCY OPERATING COSTS

FY 1964-65 to FY 1979-80



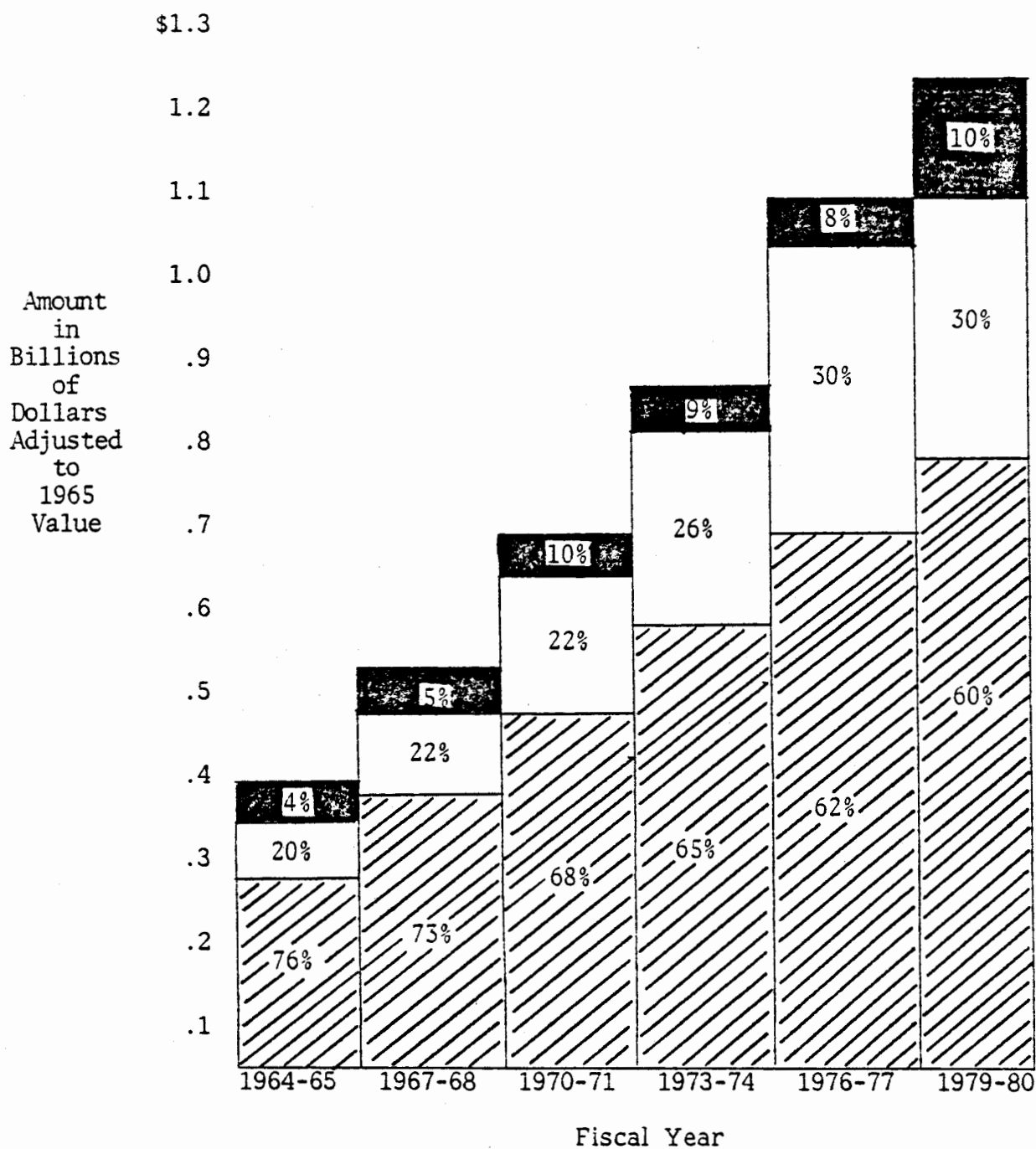
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

A - Total State Agency Expenditures.

B - Total State Agency Expenditures in Constant Value 1965 Dollars.

Source: State Budget Documents.

GROWTH IN AGENCY EXPENDITURES BY SOURCE OF
FUNDS ADJUSTED TO 1965 CONSTANT DOLLAR VALUES



-  State Funds
-  Federal Funds
-  Other Funds

Source: State Budget documents.

REPORT SUMMARY

Introduction

Because of recent changes directed at improving the budget process South Carolina is in a unique position to make significant advances in legislative oversight in the next few years. For example, within the State Budget and Control Board the recently established Grants and Contracts Review Unit and the State Planning Office have been placed under one director with the Budget Development Office. The State is implementing a modernized accounting and reporting system, and management reform legislation has become a high priority. Careful coordination of these events will be a major factor in the success of the budget process in allowing legislative oversight. This report provides recommendations to assist and promote the trend of budget reform which the General Assembly has initiated.

Specifically, this report contains a review of various aspects of the State's budget process primarily related to the implementation of Act 651 of 1978 and Part I, Section IA of the Appropriation Act for 1977-78. Chapter I contains the Legislative Audit Council's evaluation of recent budget revisions and recommendations as required by Act 651. In Chapter II the Council reviews agencies' justifications of requested expenditures required in the 1977-78 Appropriation Act. A discussion of related budget issues is contained in Chapter III.

In conducting this review an attempt was made to contact all interested parties for their information. The Council surveyed all members of the General Assembly, various State officials, and 26 agency directors regarding the new budget procedures. Various elected officials

and staff members from the State Offices of Budget Development, Planning, Grants and Contracts Review, the Auditor, Data Processing and the Comptroller General were interviewed and information gathered. The research staffs of the House Ways and Means Committee, Senate Finance Committee and the Governor's Office were also contacted to provide information on the budget process. The Council appreciates the cooperation and assistance given by the many State officials and staff in developing this report.

Additionally, a review of the State's accounting and reporting system was performed. Twenty-two State agencies' budgets were studied to determine how well the agencies were preparing the new program budget. The Council also compared the State's new budget format with those of eight other states and observed budget hearings conducted by the Budget and Control Board in September and October 1979.

Summary

Chapter I - Act 651 of 1978

Act 651 revised the format and content of the General Appropriation Act and directed State agencies to develop program budgets which contain clear descriptions of program objectives, costs and measurements of effectiveness. The structure of the Appropriation Act for FY 78-79 was expanded to show both State and Total Funds at each stage in the legislative process.

In addition, the Act established the Joint Appropriations Review Committee (JARC) as a permanent committee. This committee is responsible for determining modifications to the structure and content of the General Appropriation Act and the annual State Budget. The committee

has the added responsibility of providing legislative oversight over the expenditure of funds over and beyond those appropriated out of the General Fund. In FY 78-79 the JARC reviewed 1,258 requests for Federal grants totaling \$883,604,434 in Federal funds, \$172,521,555 in State funds and \$32,424,727 in other funds for a total of \$1,088,550,716.

The Council concludes that the General Assembly can further strengthen oversight and accountability in several areas.

- Further study should be made of matching requirements and maintenance of effort requirements on Federal grants to improve oversight of these funds by the General Assembly. Without full implementation in these areas the General Assembly is not aware of all options when funding Federal grant programs. (page 16)
- The Board and JARC should determine if State agencies are incurring a continuing obligation to the State when they accept Federal funds. The Board and JARC should review all Federal research grants to decide whether to continue to allow the exemption of these grants from the review process and requirement to recover indirect costs for remittance to the General Fund. (page 20)
- State policy should require the recovery of all allowable indirect costs on Federal grant programs. State-level oversight is needed in the development of agency indirect cost proposals to ensure full and equitable indirect cost recovery. For example,

such a policy could result in an estimated \$11.4 million being returned to the General Fund for FY 80-81 rather than the \$8.3 million shown in the State's budget document. (page 22)

- To improve the State's program budgeting system refinement of program definitions and categorization of agency programs is needed. Agencies' administrative costs can be more clearly reported for the determination of program costs. (page 26)
- Training seminars for State agency managers should be conducted by the State Auditor's Office to develop consistent program objectives and performance indicators for the 1981-82 budget. (page 32)
- The budget format submitted by agencies can be improved by changing the revenue receipts detail schedule to show individual sources of revenue and displaying it immediately after agencies' expenditures detail. (page 40)

Chapter II - Justification of Expenditures

The Audit Council was requested to determine if State agencies were justifying the full amount of their budget requests as required in the annual Appropriation Act. In order to make such an assessment this chapter focuses on three aspects of the budget cycle...preparation, execution and control. The Council found four areas where the State's system can be improved.

- More detailed budget analysis is needed. The present system of allocating a "slice of the pie" of the preliminary revenue estimate is not conducive to in-depth analysis of agencies' recurring expenses. Agencies are primarily required to justify the amount they request in excess of their allocation, while the allocation is not clearly justified. Guidelines are needed to ensure that in-depth analysis is performed and close coordination of information among the Budget and Control Board's Offices of Planning and Budget Development, and the Grants and Contracts Review Unit will be necessary.
(page 44)
- Budget hearings can be conducted to focus more on agency justification. Audit Council staff attended 42 of 55 agency budget request hearings during September and October 1979. These hearings did not always concentrate on gathering evidence and taking testimony to justify the need for public funds. There was very little questioning of agencies' recurring expenses. Some agencies were allowed to present slide shows, show fossils, demonstrate relics and spend time which did not clearly focus on justification. In-depth budget analysis would allow the preparation of alternatives and a more structured, to-the-point, hearing process. (page 49)

- Improved control and justification of agency transfers can be achieved. Data concerning the types of transfers and their effect on legislative intent is not readily available in the present State system. A material movement of State funds occurs during the budget year. For instance, during FY 78-79 \$79,247,000 of State funds were transferred for various purposes. The Council's review of justifications for transfers indicates that improved analysis and quarterly monitoring of transfers would provide better oversight and control of funds. (page 53)
- A review of the current budget reveals that agencies are continuing to underestimate their Federal and other funds by 7%. This means agencies had 7% more funds to expend during the year than recommended by the Budget and Control Board. Underestimations are understandable since agencies prepare their budgets many months in advance without final Federal funding information. The significance of this, however, is that interim information about the changes in agency budgets should be available. A budget amendment process should be instituted to control the level of expenditures and increase agency accountability to the General Assembly over State and Federal funds. (page 61)

Chapter III - Related Budget Issues

During the course of its study the Council reviewed some areas related to the budgetary process which may also require further legislative attention.

- The capabilities of the new Statewide Accounting and Reporting System (STARS) were reviewed but the system will not be implemented until FY 80-81. The implementation, operation and use of the system should be considered for in-depth review. (page 63).
- Currently the State has a total Capital Improvement Bond authorization of \$702,524,699.19 not including State Institution and Plant Improvement Bonds. Without information on the full affects that capital improvement projects have on agencies' operating budgets, legislative decision-making capabilities are limited. Further study of capital planning and budgeting should be made. (page 64)
- Printing of the Appropriation Act has risen in cost from \$48,121.68 in 1975 to \$84,044.57 in 1979. Estimates show that an average savings of about \$15.00 per page may be realized if the requirement for a printed Act would be changed to allow the use of a certified computer printout in the budgetary process. This should also result in speeding up the budget process because turnaround time in printing should be reduced. (page 67)

CHAPTER I
ACT 651 OF 1978

Introduction

Act 651 of 1978 directed the Legislative Audit Council to "conduct a review and evaluation of the revised budget process and procedures" and report its findings to the Budget and Control Board and the Joint Appropriations Review Committee (JARC) by January 8, 1980.

The Act required revisions in the format and content of the General Appropriations Act to subject funds to formal legislative authorization beginning in FY 78-79. Also included were provisions to revise the State's annual budget to show the programs of all State agencies. Agencies were required to include in their budgets clear descriptions of program objectives and costs, and measurements of program effectiveness.

Additionally, Act 651 provided for the continued operation of the Joint Appropriations Review Committee and required agencies to obtain approval of the State Budget and Control Board, and concurrence of approval from the JARC, prior to expending any funds other than those from the General Fund. A copy of Act 651 of 1978 may be found in Appendix A of this report.

This chapter addresses sections of the Act where specific actions could be taken, and those actions are assessed as to the degree of compliance with the Act. Also recommendations are provided to improve legislative oversight in accordance with the intent of the Act.

Sections 1 and 2

Sections 1 and 2 establish the General Assembly's intent to "modify the structure of the state general appropriation act so as to specifically authorize and control the expenditure of those funds involved in the operation of state government over and beyond those appropriated out of the general fund, and that the modifications would become effective with the general appropriation act for 1978-79."

The structure of the Appropriation Act for FY 78-79 was expanded to show both State and Total Funds as required at each stage in the legislative process. Prior to that year, only State funds were shown.

Section 3

In Act 219 (1977) the General Assembly created a joint legislative committee to be responsible for determining modifications to the structure and content of the annual State General Appropriations Act and the format of the annual State Budget. Act 651 (1978) established this committee as a permanent committee to be known as the Joint Appropriations Review Committee with the additional responsibility of providing legislative oversight for the expenditure of funds over and beyond those appropriated out of the General Fund.

The JARC consists of three members from the Senate Finance Committee and three members from the House Ways and Means Committee. The members are appointed by the chairmen of the two committees. Current members of JARC are Senators Allen R. Carter, Robert C. Lake, Jr. and Harris P. Smith and Representatives Thomas W. Edwards, Patrick B. Harris and David F. McInnis.

Sections 4 and 5

Act 651 specifically required the Joint Appropriations Review Committee (JARC), in concurrence with the Budget and Control Board, to approve or deny agency proposals to expend Federal and other funds over and above those appropriated out of the General Fund, thus subjecting all funds involved in State Government to legislative authorization. The Board, in cooperation with the Committee, was directed to make such rules and procedures as might be necessary to carry out this function.

The Legislative Audit Council interviewed the Director of the Grants and Contracts Review Unit, and reviewed the minutes of the JARC and the Budget and Control Board to determine compliance with Act 651. JARC had its initial meeting on August 8, 1978 and no minutes were available for meetings held from then until the start of the next legislative session in January 1979. Between January 16, 1979 and November 2, 1979, the Committee met 20 times.

Members of the JARC appeared to be well-prepared for meetings, having carefully reviewed agency requests. Committee diligence is evidenced in the minutes of the March 27, 1979 meeting when it was suggested that projects with small dollar amounts be given automatic approval. The consensus of the Committee was that they were still in the learning process and should review all requests in order to consider all aspects of Federal programs.

Bulletin No. 79-5 of the Advisory Commission on Intergovernmental Relations entitled "State Legislative Oversight of Federal Funds: An Update in Brief" outlined the process in Pennsylvania, California, Oregon, South Dakota and Illinois. South Carolina's present system

compares favorably with Oregon's, which is cited by the Commission as a "success story."

The Council found that the procedures followed were in accordance with Act 651. When the General Assembly is in session the agencies submit their requests to the Grants and Contracts Review Unit (GCRU) which makes a recommendation on each one. A Budget and Control Board subcommittee, comprised of the Governor, Treasurer and Comptroller-General, reviews the requests and the GCRU recommendations and presents its conclusions to the full Board for action. The Board furnishes the requests and its recommendations to the JARC for concurrence or nonconcurrence. When the General Assembly is not in session the GCRU furnishes the agency requests and its recommendations to the JARC, which makes its review and furnishes the Budget and Control Board with its advice or recommendations. The Board then makes the final decision.

The Legislative Audit Council found that at no time has the Board acted against the wishes of the Committee. When there were points of nonconcurrence the JARC and the Board resolved them so that agreement could be reached and recommendations made.

According to the records of the GCRU, for FY 78-79, 1,258 project requests were received, concerning \$883,604,434 in Federal funds, \$172,521,555 in State funds and \$32,424,727 in other funds, for a total of \$1,088,550,716. No reports are generated on projects and dollars which are disapproved, but this information can be obtained by looking through each individual packet of requests or consulting the GCRU files which contain a log on each requesting agency. The Audit Council reviewed logs on 76 agencies in the GCRU files and found that denied

requests for FY 78-79 involved \$416,601 in Federal funds and \$92,682 in State money. These denials amounted to .05% of requests for Federal funds for that year.

Need to Improve Grant Matching Information

Although the State has established a procedure for approving and reporting the award of a Federal grant, this system does not achieve adequate oversight in regard to State matching requirements. The system is not equipped to track the progress of a Federal grant to ensure that the amount requested by an agency is the same amount it receives and that Federal and other funds are expended prior to State matching funds.

Once an agency's request is approved by the JARC and the Budget and Control Board, the agency makes application to the Federal agency for the grant. The law requires agencies to report within 14 days the approval or rejection of a grant application by the Federal Government and whether or not a change in the amount awarded has occurred. However, actual receipts are not reported until agencies submit their next year's budget request. Currently, the Comptroller General sets up Federal funds in a single account for each agency, such as "Consolidated Federal," therefore these State records do not provide individual grant information. However, when implemented, the Statewide Accounting and Reporting System (STARS) is expected to provide individual grant program information.

Federal programs generally allow two kinds of match..."hard" match (or cash) and "soft" match (or in-kind contributions). More often a cash match is required. Monitoring the use and requirements of

match at the State level is a complex task but is crucial to legislative oversight.

Hypothetically, an agency may receive approval for a \$750,000 grant award and a General Fund appropriation of \$250,000 to meet a 25% matching requirement, the total grant cost therefore would be budgeted at \$1,000,000. During the grant period, if a reduction in Federal funds occurred the Legislature would have no easy way of reducing the State match proportionately. While it may be argued that the Legislature authorized the agency to spend \$250,000, it is also true that the \$250,000 was authorized to meet the minimum matching requirement. If the Legislature was aware that Federal funds had decreased, a proportionate decrease of State match may be desired for that grant program. However, if such an alternative is not brought to the attention of the Legislature, it cannot be considered, whether or not desirable.

Section 130 of the annual Appropriation Act addresses the issue of State agencies using matching funds for Federal grants. The section states:

All Federal Funds received shall be deposited in the State Treasury, if not in conflict with Federal regulations, and withdrawn therefrom as needed, in the same manner as that provided for the disbursement of state funds. If it shall be determined that federal funds are not available for, or cannot be appropriately used in connection with, all or any part of any activity or program for which state funds are specifically appropriated in this Act to match Federal funds, the appropriated funds may not be expended and shall be returned to the General Fund.

In addition, Section 124 of the annual Appropriation Act stipulates that Federal and other money will be spent before State funds:

All departments, institutions and agencies of the State having revenue funds other than State appropriated funds available for operations, shall use

such revenue before appropriations from the State's general fund are expended or requisitioned.

Since matching funds are seldom itemized or "specifically appropriated" in the Appropriation Act, and Federal grants are rarely distinguished by individual State-level accounts, the State is without adequate information to determine if Sections 124 and 130 are followed unless an audit were to disclose a problem.

Additionally, Federal grant programs usually have a "maintenance of effort" requirement for states to be eligible to receive funds. This, for example, may require that a state could not spend less state money than was expended in a previous base year for the same kind of services to be provided under the grant program. Such a requirement is to prevent states from "supplanting" or substituting Federal funds for a previously state funded program or service. However, the base year for determining the minimum level of state funding may be several years ago and in the meantime the state could have far surpassed that minimum requirement. Therefore, the Legislature could, in some cases, not increase state spending for a particular program and continue to be eligible to receive Federal funds. Such a determination can be made when adequate information concerning maintenance of effort is known.

The present system limits the choices by the General Assembly when funding Federal grant programs because the availability and quality of information provided to legislators is not adequate. Without adequate information the Legislature is not fully aware of alternative funding choices regarding Federal grant programs.

RECOMMENDATION

THE JOINT APPROPRIATIONS REVIEW COMMITTEE AND THE STATE BUDGET AND CONTROL BOARD SHOULD ENSURE THAT FURTHER STUDY IS MADE TO DETERMINE HOW THE GENERAL ASSEMBLY CAN IMPROVE OVERSIGHT OF MATCHING REQUIREMENTS AND MAINTENANCE OF EFFORT REQUIREMENTS.

IN THE MEANTIME, CONSIDERATION SHOULD BE GIVEN TO USING THE ACTUAL FEDERAL AND OTHER FUNDS REPORTED IN AGENCIES' BUDGET REQUEST DOCUMENTS AND/OR REQUIRING THAT ACTUAL GRANT AWARDS AND RECEIPTS BE REPORTED PERIODICALLY DURING THE YEAR.

Section 6

Section 6 of Act 651 of 1978, gives the Budget and Control Board and the Joint Appropriations Review Committee (JARC) the authority to review separate Federal grant programs which are under the supervision of one designated agency or a newly established commission or board. The Act states that the Board or the JARC, "shall determine the requirement or desirability for a single agency designation. If the designation is found to be desirable or required the Board or Committee, with the concurrence of the Board or Committee in accordance, shall make the designation,..."

Various Federal Regulations require that either a "single State agency" be designated or a board or commission be established to

supervise the administration of Federal grant programs. The purpose of such a designation is to increase efficiency, control, and uniformity in the flow of Federal funds into a state. In accordance with the Federal Intergovernmental Cooperation Act of 1968, the Governor, or appropriate legislative authority of a state, may request a waiver of the single state agency designation. If it can be shown that such a designation is not the most effective and efficient organizational arrangement within the State Government and that the objectives of the Federal statute will not be endangered, then the Federal department head may approve the waiver.

Section 6 of Act 651, is a mechanism whereby the General Assembly has direct input into the process of designating "single state agencies" or determining that a single state agency designation would not be desirable. As of December 1979, the Council found no instances where the State Budget and Control Board or the Joint Appropriations Review Committee found it necessary to make recommendations in accordance with this section of State law.

Section 7

Section 7 establishes criteria for State agencies applying for Federal research grants or student loan funds. The section states that acceptance of a grant must not, "create a continuing obligation to commit State funds or State resources beyond the term of the grants." Although the law does allow this exemption, State agencies and institutions are required to report to the Board and the JARC the receipt of a Federal research grant within 14 days. This section exempts research grants and student loans from prior review and approval by the Budget and

Control Board or the Joint Appropriations Review Committee (JARC) as required of other Federal grants. It also exempts agencies from remitting indirect cost recoveries of research grants to the State General Fund.

Currently it is unclear how the State could detect if an agency is incurring a continuing obligation when it receives a Federal research grant. Presently the only defined check on continuing commitments is the requirement that the agency file appropriate GCRU forms if State funds or resources will be used beyond the grant period. Such commitments include direct or other obligations such as the maintenance of facilities and equipment. In addition, agencies must report a full explanation of how indirect cost reimbursements will be used. The law does not specify that the State should develop further controls, post audit for example, that would ensure that agencies are not incurring a continuing obligation when they accept a Federal research grant.

As of August 13, 1979 the Grants and Contracts Review Unit (GCRU) reported that 13 State agencies and institutions received 331 research grants and 56 student loan funds in FY 78-79. These grants totaled \$23,426,111, while a total of \$2,930,503 of indirect cost recoveries was retained by the State agencies and institutions.

RECOMMENDATIONS

THE BOARD AND JARC SHOULD COMMISSION A STUDY TO DETERMINE HOW THE STATE CAN MONITOR THE ADMINISTRATION OF FEDERAL RESEARCH GRANTS AND STUDENT LOAN FUNDS TO ENSURE THAT STATE AGENCIES ARE NOT INCURRING A CONTINUING OBLIGATION WHEN

THEY ACCEPT THESE FUNDS. THIS STUDY SHOULD ALSO REVIEW THE USE OF INDIRECT COST RECOVERIES TO DETERMINE IF ALL FEDERAL RESEARCH GRANTS AND STUDENT LOAN FUNDS SHOULD CONTINUE TO BE EXEMPTED FROM REMITTANCE TO THE GENERAL FUND.

Section 9

Section 9 of Act 651 allows the Budget and Control Board or the Joint Appropriations Review Committee (JARC) to waive the requirement that Federal indirect cost recoveries be remitted to the General Fund by State agencies.

The Council reviewed the minutes of the Board for the past two fiscal years and the minutes of the JARC for the past fiscal year, the first year of its existence. Neither the Board nor JARC have recommended that a waiver be granted. This practice has set a precedent which makes agencies aware that the State will require that indirect costs be recovered and remitted to the General Fund without exception.

Need to Recover Full Amount of Indirect Costs

State law and the efforts of the State Budget and Control Board and the Joint Appropriations Review Committee have significantly improved legislative control of indirect costs. However, effective oversight of indirect costs continues to be hindered because State agencies are not required to recover the full amount of indirect costs for the Federal programs they administer. During FY 78-79 in compliance with State law, \$6.4 million of indirect cost reimbursements were deposited

into the State General Fund and brought under the direct control of the Legislature.

For FY 80-81 the estimated indirect cost recovery shown in the budget document is \$8.3 million. This estimate is based on agencies' projected recoveries. However, an estimate for the same period prepared by the State Grants and Contracts Review Unit, indicates that an estimated \$11.4 million could be returned to the General Fund if agencies' indirect cost rates were fully developed, and the amount of Federal funds estimated is received.

Many State agencies are given the responsibility for administering Federal programs. All such programs have two basic categories of costs; those incurred to provide services (direct costs) and those incurred to administer the program (indirect or overhead costs). Federal Regulations allow State agencies to use a portion of their funds for the costs of administrative overhead. To do this, the agency must file a proposal and obtain Federal approval for an "indirect cost rate." With this rate applied to direct costs the agency can use Federal funds to pay for administrative costs, including some of the costs incurred by other central State agencies (such as the State Treasurer's Office and the State Comptroller's Office).

In a previous study of The Impact of Federal and Other Funding on Legislative Oversight, the Legislative Audit Council recommended that agencies should be required to develop, obtain approval, and implement indirect cost allocation proposals. The proposals should include all allowable statewide indirect costs and all allowable indirect costs of the agency for which the proposal is prepared. Presently the State requires that an agency submit a proposal, however, the agency has the option of which method to use, and how much to claim. The agency needs only to seek approval of its proposal of its "cognizant Federal agency"

(generally the Federal Department which has the greatest dollar investment in the programs administered by the agency). There is currently no central State office designated to work with and assist the State agencies in formulating their proposals; they must rely instead on Federal officials. One such official commented that the majority of the State agency personnel who are responsible for the indirect cost proposal are "not knowledgeable enough to negotiate a fair rate." Without guidance from an independent and knowledgeable representative of the State, indirect cost proposals will often reflect a rate more favorable to the Federal Government rather than a rate that permits the Federal Government to pay its fair share.

Neither State law nor policy require the full recovery of indirect costs. Section 13 of the 1978-79 Appropriation Act states..."it is the intent of the General Assembly that where expenditures of State funds are reimbursed by Federal or other funds, ...such reimbursements shall be returned to the General Fund of the State (and)... shall include... various indirect and overhead costs recoveries..." In addition, the Budget and Control Board has established a policy which does not specifically require full indirect cost recovery:

...indirect cost recoveries must be applied for where permitted under Federal Regulations, and must be deposited in the General Fund as required in the current Appropriations Act.

In March 1979, the Federal General Accounting Office (GAO) issued a report on the recovery of indirect costs for Federal grants and contracts. The report, Federal Cost Principals are Often Not Applied in Grants and Contracts with State and Local Governments, found that indirect cost plans and proposals are improperly prepared and used by State and local governments. The report stated, "Improperly prepared

cost allocation plans, on the other hand, can adversely affect the grantee's recovery of legitimate joint costs."

The report also found that some Federal and State grant-making officials, "do not agree that indirect costs applicable to a project should be paid." The officials argued:

- (1) limited Federal funds are better used for direct program purposes,
- (2) grantees have normally absorbed such costs in the past, and
- (3) grantees do not necessarily incur additional indirect costs when undertaking federally assisted projects.

The GAO concluded:

Actions based on attitudes of this nature help explain why State and local government grantees are not systematically identifying indirect costs applicable to federally assigned programs.

Since all indirect cost recoveries must go directly to the State General Fund rather than into agency programs, there is less incentive for an agency to claim all eligible indirect costs. Therefore, from the agency's perspective, it is sometimes more advantageous to seek the lowest possible rate rather than the most equitable.

At a time when the State is moving toward accounting and budgeting on a program cost basis, the need to identify the indirect costs of programs becomes increasingly important so that the full cost of services may be known. If an agency has the option to recover indirect costs and neglects to do so, an additional burden is placed on South Carolina's taxpayers and the General Fund to pay more than a fair share for administering federally funded programs. In effect, this denies the General Assembly its right to decide how State funds will be used. Until the proper amount of indirect costs are identified for each agency this circumvention of the legislative budget process will continue.

RECOMMENDATIONS

THE STATE BUDGET AND CONTROL BOARD AND
THE JOINT APPROPRIATIONS REVIEW COMMITTEE
SHOULD:

- (1) PROVIDE TECHNICAL ASSISTANCE TO
AGENCIES IN DEVELOPING INDIRECT
COST ALLOCATION PROPOSALS, AND
- (2) OVERSEE OR CONDUCT THE NEGOTIA-
TIONS FOR INDIRECT COST RATES
BETWEEN STATE AGENCIES AND FEDERAL
AGENCIES TO ASSURE THAT AN EQUI-
TABLE RATE IS ATTAINED.

EITHER STATE LAW OR STATE POLICY SHOULD
REQUIRE ALL AGENCIES TO RECOVER ALL ALLOW-
ABLE INDIRECT COSTS.

Sections 10 and 11

Introduction

Section 10 of the Act directed the Budget and Control Board to revise the annual budget document so as to "present a format which clearly delineated each agency's and institution's programs, their sources of revenue, the associated program objectives, the total program costs and program effectiveness measurements." Moreover, Section 11 of the Act required the "full cooperation" of all agencies and institutions in making these revisions.

South Carolina's change to a program budget is in its early stages. Statewide program functions have yet to be incorporated into the structure, the budget format needs further refinement and performance measures of various agencies have not been used long enough to indicate trends. Therefore, it would be premature to attempt to evaluate the impact of program budgeting on the State's planning capability and its impact on the Legislature's ability to allocate the State's resources.

In September 1978, the Budget and Control Board adopted a revised budget format for the 1979-80 budget document with the approval of the Joint Appropriations Review Committee. The revised format included the Act 651 parameters and required efficiency statistics in addition to effectiveness measures.

To determine compliance with format revisions, LAC reviewed a sample of agency budget documents for 1979-80, using a random start and every fifth agency thereafter (alphabetically), for a total sample of twenty-two agencies. LAC also reviewed the budget request formats of eight other states; North Carolina, Georgia, Tennessee, Kentucky, Florida, Mississippi, New Hampshire and California, for comparative purposes.

The Legislative Audit Council sent a survey to all State legislators regarding the revised format of the budget document. Approximately 58% of the legislators who responded indicated they were satisfied with the overall format revisions, however, only 30% felt they could determine the costs of programs to their satisfaction. Forty-four percent (44%) felt agency programs were clearly defined, 33% felt program objectives were clearly presented, 70% felt source of funds information has been improved, and 69% felt the effectiveness and efficiency measures provided useful information.

Summary

The Joint Appropriations Review Committee and the Budget and Control Board are in compliance with Act 651, in that a revised format was devised under the auspices of the Budget and Control Board and approved by the Joint Appropriations Review Committee. The revised format provides for the parameters required by Act 651. The LAC sample showed that agencies had complied with the revised format as set forth in the 1979-80 South Carolina Budget Preparation Manual. However, there is a need for more research into program definition and formulation, coupled with the need to improve performance measures and objectives. As a result budget requests, although in compliance, are not yet providing fully useful information. The following paragraphs provide further details and recommendations where appropriate.

Program Format

Act 651 required a program budget format for the 1979-80 budget document. Prior to 1979-80, South Carolina had traditionally oriented the budget format to the organizational structure of the agency. The primary purpose of the traditional format was to impose accounting and administrative responsibility upon department or division heads who expend the State's funds. Without modification it does not show total expenditures for specific services, functions or activities which are components of the program concept.

Program budgets deal principally with broad planning and the costs of functions or activities. They require accounting for the total cost of a program statewide, regardless of the organizational units

(agencies) which may be involved in carrying such programs into execution. Budget data is arrayed and analyzed in terms of meeting State goals and public needs.

If a policy issue crosses agency lines, the program classification facilitates the accumulation of cost and other information as needed. It allows planning related to need on a broad basis and can be used to detect or prevent unnecessary duplication. The program structure is designed to provide a systematic way of accumulating and presenting costs to meet the needs of decision-makers. South Carolina currently does not have the accounting capability to support a full program budget since there is no statewide program classification system. However the Statewide Accounting and Reporting System (STARS) is expected to include this capability.

Act 651 required a modified program format for budgets beginning with the 1979-80 budget year. That is, data was organized solely within major organizational units (agencies), with no statewide classifications across agency lines.

Since the Act was passed in July 1978, there was little time to prepare careful and detailed explanations of the program concept for the 1979-80 Budget Preparation Manual (which was distributed in July 1978), and indeed, no explanation appeared. The sample forms which appeared in the Manual used the Children's Bureau as an example, and included a Program Chart which was identical to the previous year's Organizational Chart. This, along with the fact that many of the previous organizational divisions were already based on functional lines, explains why 10 of the 22 agencies in the LAC sample showed no difference between their Program Chart and their previous Organizational

Chart, thus no change in their cost accumulation centers. The other 12 agencies included some change in degree of detail, some renaming of essentially similar functions, and, in two cases, some re-aligning of cost centers.

A program may be defined as a category of similar services directed at meeting certain related public needs. It answers the question, "What services are provided for whom?" The Children's Bureau, given as the example in the 1979-80 Budget Preparation Manual, had three divisions in 1978-79; Administration, Child Care, and Work with Natural Parents and Adoptive Families. Although the latter two divisions were based on program lines (providing specific services to others) it may be argued that the first division, Administration, was not clearly a program. Administration may be viewed as a management function rather than an agency program, with the purpose of providing a support system for agency programs. Without this support it would be difficult, if not impossible, to carry out the programs. Therefore, to arrive at a valid total program cost, the cost of administration could be included as a part of an agency's programs. Some administrative costs may be linked directly to a specific program, and some must be indirectly allocated among the programs of an agency.

The administrative cost for an agency is useful management information and should be available as separate information. The STARS system is expected to provide several levels of organizational detail in addition to program classifications, allowing the presentation of administrative costs both as applied to programs and as a total for each agency.

The 1979-80 format included Employee Benefits as a part of each program, which is in keeping with accumulating costs by program.

However, the 1980-81 format shows Employee Benefits as a separate program. Employee Benefits are clearly not a program, but rather are linked directly with Personal Services. Just as Personal Services costs are accumulated by program, also should Employee Benefits be accumulated by program.

In summary, implementation actions by the Budget and Control Board have brought us part of the way to a program budget. If the Legislature desires a full program approach to budgeting, a detailed study of the program structure of the State may be necessary. Statewide program functions have been identified by the State Planning Division. The next task would be to classify each agency's programs along these statewide lines.

RECOMMENDATIONS

THE JOINT APPROPRIATIONS REVIEW COMMITTEE
AND THE BUDGET AND CONTROL BOARD SHOULD
HAVE AGENCY ADMINISTRATIVE COSTS REPORTED
IN TWO WAYS:

- (1) AS A SEPARATE PROGRAM FOR ORGANIZATIONAL CONTROL, WHICH IS CURRENTLY DONE.
- (2) AS ALLOCATED TO EACH AGENCY PROGRAM TO PROVIDE TOTAL PROGRAM COST INFORMATION. THIS COULD BE DONE ON A SEPARATE FORM AND MAINTAINED BY THE BUDGET

OFFICE FOR ANALYSIS, OR COULD BE INCLUDED
IN THE BUDGET DOCUMENT IMMEDIATELY
AFTER THE ADMINISTRATIVE PROGRAM
EFFICIENCY MEASURES.

EMPLOYEE BENEFITS SHOULD BE APPLIED TO
EACH AGENCY PROGRAM TO PROVIDE ACCURATE
PROGRAM COST INFORMATION.

REFINEMENT OF PROGRAM DEFINITIONS AND
CATEGORIZATION OF AGENCY PROGRAMS SHOULD
BE CONTINUED TO ALLOW IMPROVED STATEWIDE
PROGRAM INFORMATION.

Program Objectives

Based on agency budget requests South Carolina is currently faced with more needs than the State has resources to fund. The challenge, then, is to evaluate the need for, and effectiveness of, the services the State provides. Once the budget is structured along program lines, program performance measurements should provide important information for legislative use in making policy decisions regarding the allocation of scarce resources.

Setting program objectives is a critical part of the budgetary process, because the objectives become the foundation for program work. The formulation of objectives begins with law. Legislative intent, or the role and purpose of an agency, must first be expressed in writing as goals. Goals are not usually expressed in measurable

terms but can be viewed as the statement of purpose which keeps an agency's efforts directed toward meeting the need the Legislature intended. An agency expresses the accomplishment of its goals in measurable objectives. Objectives may be subdivided into quantifiable statements (performance indicators) which measure compliance, efficiency, economy, and effectiveness. Objectives which do not reflect the full scope of these measures cannot provide an adequate perspective of the results achieved by an agency or a particular program.

LAC's review of budget preparation material from other states indicates that the most useful type of objective is one which specifies a single key result by a target date, answering the questions "what" and "when" and being output oriented.

The Georgia Office of Planning and Budget gave an example of a statement of program purpose and a corresponding objective as follows:

Purpose: To investigate departmental equal employment opportunity complaints and to implement the department's Affirmative Action Plan in conformity with Federal guidelines to insure equal employment opportunity in State Government.

Objective: Decrease the number of equal employment opportunity complaints by 30% (from 15 to 10) in FY 77 and increase departmental minority employment by 10% (from 1,128 to 1,240) in FY 77.

Kentucky gave a sample format as follows:

<u>To</u>	<u>Action Verb</u>	<u>Subject</u>	<u>Fiscal Base Period</u>	<u>By</u>	<u>Rate/ Amount</u>	<u>Time</u>
To	decrease	# of fatal accidents per 1,000 passenger miles	1980	by	5%	6/30/81
To	increase	# of accommodations available for overnight campers in Kentucky State parks during	1980	by	2,500	6/30/81

The 1979-80 and 1980-81 South Carolina Budget Preparation Manual instructions were much less precise, requesting that program objectives (1) describe the most important activities of the program, (2) be clear, concise and understandable, and (3) be measurable, so that the degree of obtainable objective (performance) can be ascertained. In the sample forms, none of the objectives was shown in the form of specific, measurable accomplishments. It is not surprising, then, that the program objectives submitted by the agencies in the LAC sample were generally not very useful in analyzing their program accomplishments. They were more like narrative activity descriptions than expressions of "hoped for" results in numerical terms. The 1980-81 South Carolina Budget Preparation Manual commended the agencies on their efforts to comply with new requirements and then added: "There have also been varying degrees of semi- or non-compliance. A mass of figures without worthwhile statements of objectives in measurable qualitative and quantitative terms is almost meaningless as a management tool."

Of all the objectives in all 22 agencies in the LAC sample, none was as precise as in the form suggested by the Georgia and Kentucky examples. Vague words were used such as "plan," "coordinate," "monitor" and "insure." A common objective listed was "efficient and timely processing," with no indication as to what is considered efficient and what is considered timely. Following the examples given in the 1979-80 South Carolina Budget Preparation Manual, the specific achievements for which the agencies were striving were shown as part of the measurements rather than part of the objectives (see next section).

Displaying objectives in the format suggested by the Georgia and Kentucky examples is not a panacea. Not all agency functions can be

expressed in terms of measurable output, and quantified objectives do not guarantee greater control. However, the formats noted do force logical thinking and careful examination of a program's functions.

Program Effectiveness and Efficiency Measures

Once program goals have been expressed as specific objectives, performance indicators are needed. The two basic types of indicators are effectiveness measures and efficiency measures.

Effectiveness measures relate program results to program objectives by measuring the degree to which the objective was attained. For instance, if one of an agency's objectives was "to increase the number of new manufacturing jobs in South Carolina by 10,000 during the budget year," the related effectiveness measure would be "number of new manufacturing jobs created in South Carolina, projected and actual."

Efficiency measures relate to the cost of reaching program objectives. They are most typically expressed as unit costs, that is, the cost of producing one unit of output. Using the example above, a related efficiency measure would be "average cost of attracting one new manufacturing job to South Carolina."

The 1979-80 South Carolina Budget Preparation Manual required efficiency and effectiveness measures for each program. The examples given for the Children's Bureau were clear, understandable and quantified. However, for the Children's Bureau program of Administration, one example measurement was "number of vouchers processed." It is difficult to see how this related to the effectiveness of the program unless a program objective was to process a certain number of vouchers.

It should be noted that one of the objectives included in the program of Administration for the Children's Bureau was "efficient and timely processing" with no related measurements of "efficient or timely." This nebulous objective was picked up by many of the agencies in the LAC sample, also with no related measurements, and used in programs other than Administration.

Since objectives in the South Carolina Budget Preparation Manual were not set up in the form of quantified target results, the effectiveness measures became the objectives, showing actual results for 1977-78, budgeted results for 1978-79 and expected results for the budget request year, 1979-80. The problem becomes one of clarity, as it is difficult to determine what the agency sees as its specific goal. Using the "new manufacturing jobs" example, the objective of increasing the number by 10,000 is easier to understand than an objective of attracting new manufacturing jobs followed by an effectiveness measure such as "announced new manufacturing jobs in South Carolina" 77-78/15,111; 78-79/11,800; 79-80/12,600.

The agencies in the LAC sample were basically in compliance with the measurements as required by the 1979-80 South Carolina Budget Preparation Manual. However, the quality of the statistics as well as the format could be improved. In particular, the measurements were frequently difficult to relate to the objectives. For instance, one of the Medical University of South Carolina's objectives was "to maintain an intellectual and professional environment for education." The effectiveness measure used was "number of health care students." The Board of Social Workers Registration included as an efficiency measure, "number of Board members."

The format used was a list of objectives followed by a list of effectiveness measures followed by a list of efficiency measures. There was no clear relationship shown between the objectives and the performance indicators. If the format were changed to show the objective followed immediately by its effectiveness and efficiency measures the relationship would become clearer. Clemson Public Service Activities was the only agency in the LAC sample that did this. Another possible way to relate performance indicators to objectives would be to number the objectives and number the indicators to correspond. The process of determining these relationships would exert pressure on agency management to refine their objectives and devise valid measurements, eliminating some unimportant statistics in the process. Once the system is refined the performance indicators should provide, in addition to a tool for legislative evaluation of programs, valuable management information, especially if management provides for a feedback system within the agency to monitor progress toward meeting objectives during the budgeted year.

In conclusion the following criteria should be considered for selecting measures of efficiency and effectiveness in order to obtain the most relevant measures for the program:

- (1) Appropriateness and Validity. Does the measure relate to the program's objectives for that service and does it really measure the degree to which a need or desire is being met - including minimization of detrimental effects?
- (2) Uniqueness. Does it measure some effectiveness characteristic that no other measure encompasses?
- (3) Completeness. Does the list of measures cover all or at least most objectives?

- (4) Comprehensibility. Is the measure understandable?
- (5) Controllability. Is the condition measured, at least partially, the program's responsibility? Does the program have some control over it?
- (6) Cost. Are cost and staffing requirements for data collection reasonable? The answer to this will depend partly on the state's funding situation and its interest in a particular measure.
- (7) Timeliness of Feedback. Information needed for setting budget levels for the coming year should be available before decision-makers reach their deadline.
- (8) Accuracy and Reliability. Can sufficiently accurate and reliable information be obtained? This is a problem not only with procedures that use samples, such as surveys, but with many government statistics, such as crime rates.

In addition, each measure should address some program characteristic not covered by any other measure. The monitoring of multiple measures is desirable to avoid excessive focus on one aspect of a service at the expense of others. Yet the cost of data collection and analysis and the need to prevent information overload are reasons for keeping the number to a minimum.

To reduce the burden of a large number of measures, there are four basic alternative approaches:

- Include only the more "global" or system-wide measures, deleting those focused on narrow service characteristics. One can, for example, obtain information on citizens' overall level of satisfaction with State parks rather than listing detailed measures. The global measures provide an important overview to upper-level officials such as agency directors, B&C Board members and legislators.
- Include measures focused on specific service characteristics and eliminate the global measures. Individual operating agencies are likely to find measurements of specific service characteristics more useful in determining needed actions.

- Include both global and specific measures but reduce their coverage. One way to do this is to exclude service characteristics judged to be of minor importance. Another possibility is to exclude measures of conditions that are deemed unlikely to change substantially from one period to another.
- Minimize the potential information overload by having agencies provide summaries for the budget document focusing on key measures and on those that show unusually high or low values.

Moreover, agencies are required to submit an Annual Report although the content of such reports is not specified. Possibly, detailed objectives and related measures could be included in Annual Reports to prevent overloading the budget document.

RECOMMENDATIONS

THE JOINT APPROPRIATIONS REVIEW COMMITTEE AND THE STATE BUDGET AND CONTROL BOARD SHOULD CONSIDER CONDUCTING A TRAINING SEMINAR(S) EARLY IN 1980 FOR STATE AGENCY MANAGERS ON DEVELOPING WRITTEN OBJECTIVES AND PERFORMANCE INDICATORS.

ALL STATE AGENCIES SHOULD BE REQUIRED TO SUBMIT TO THE STATE PLANNING AND BUDGET DEVELOPMENT OFFICES A LIST OF PROPOSED OBJECTIVES AND PERFORMANCE INDICATORS FOR EACH PROGRAM FOR THE 1981-82 BUDGET YEAR. THESE OBJECTIVES SHOULD BE REVIEWED FOR

CONSISTENCY WITH STATE LAW AND GOALS. THE APPROPRIATENESS, SPECIFICITY AND MEASURABILITY OF OBJECTIVES SHOULD BE CLOSELY REVIEWED. IF NECESSARY, THE PLANNERS AND BUDGET ANALYSTS SHOULD MEET WITH THE AGENCIES FOR FURTHER DISCUSSION AND REFINEMENT. BY JUNE 1980, ALL AGENCIES SHOULD HAVE IMPROVED, AND OBTAINED APPROVAL OF, THE OBJECTIVES AND PERFORMANCE INDICATORS FOR INCLUSION IN THEIR 1981-82 BUDGET REQUESTS.

Sources of Revenue

Section 10 requires that the State's budget structure shall be revised to delineate clearly the revenue sources of agency programs. The Budget and Control Board complied with this requirement in the 1979-80 budget document. However, the specific sources and amounts of Federal and other funds shown were presented in such a manner that made it difficult to use.

The Revenue Statement Receipts Detail is an agency summary form that itemized revenue receipts by individual sources and amounts. Each Federal fund and revenue source was separately identified, and the account number of the agency program to which it applied was shown, which was an improvement over prior years. If one revenue source was applied to more than one agency program, the amount for each program was displayed separately.

Showing agency program numbers for each individual revenue source is an important tool for evaluating agency programs. However,

the information as it appeared in the 1979-80 document was awkward to use because the facts needed for review and analysis had to be obtained from three different sections of each agency's budget request. First, the agency program number had to be obtained from the Description of Programs at the beginning of the agency's budget information. Second, the "Receipts Detail" at the end of the budget information had to be scanned for all the items relating to that particular program number. Third, program expenditure information was obtained from the "Detail of Expenditures" form.

Of the eight states whose budget material was reviewed by LAC, all except Mississippi presented detailed revenue information on the program level and all presented program expenditures and detailed revenue source information together for each program. If South Carolina changed the budget document format so as to present the detailed revenue information as part of each program's detail, the information would be easier to use. At the same time, unnecessary detail could be eliminated from the Receipts Detail schedule. This could be revised to list each individual revenue source for the agency as a whole instead of displaying each grant separately for each program.

RECOMMENDATIONS

THE BUDGET FORMAT SUBMITTED BY AGENCIES SHOULD BE REVISED SO AS TO DISPLAY EACH PROGRAM'S INDIVIDUAL FEDERAL GRANTS AND OTHER INDIVIDUAL REVENUE SOURCES IMMEDIATELY FOLLOWING ITS EXPENDITURES DETAIL. ALTHOUGH THIS DETAIL MAY NOT BE NECESSARY IN THE

BUDGET DOCUMENT, IT SHOULD BE PROVIDED TO THE LEGISLATIVE FINANCE COMMITTEES.

THE REVENUE RECEIPTS DETAIL SCHEDULE SHOULD BE REVISED TO BE ONLY AN AGENCY-WIDE SUMMARY. THE SCHEDULE SHOULD LIST INDIVIDUAL FEDERAL GRANTS AND OTHER INDIVIDUAL REVENUE SOURCES FOR THE AGENCY AS A WHOLE, COMBINED FOR ALL PROGRAMS.

Section 12

Act 651 requires the JARC to "prepare and submit to the Ways and Means Committee of the House and the Finance Committee of the Senate a comprehensive recommendation regarding any further legislative action which may be needed to implement the intent of this resolution."

The Committee has addressed itself to Section 151 of the 1979-1980 Appropriation Act which deals with "the disturbing increase in the number of personnel employed by the State of South Carolina." Additionally, they are concerned additionally with the fact that Appropriation Act figures and Budget Office figures regarding number of personnel do not agree because of a difference in the method of counting.

At the October 5, 1979 meeting, the Committee requested that the State Auditor draft procedures and recommendations to correct the discrepancies in "head count." It also discussed possible changes in Section 151 to further control growth in personnel in State Government.

Along with these actions, it is felt that this report by the Audit Council should assist JARC in developing recommended legislative actions to improve the implementation of Act 651.

CHAPTER II

JUSTIFICATION OF EXPENDITURES

Introduction

In addition to auditing for compliance with Act 651 of 1978, the Audit Council was requested to determine if State agencies were justifying the full amount of their budget requests. Section 1A, Part 1 of the 1977-78 Appropriation Act directed the Budget and Control Board to require each agency to "justify its entire budget request to include recurring as well as new or additional expenses." This provision was retained in subsequent years and made a part of the permanent provisions of the 1979-80 Appropriation Act.

Agencies' budget requests are based on an allocation system. The Budget and Control Board uses the preliminary revenue estimate for the budget year to develop an allocation for each agency based on its previous year's appropriation, adjusted for non-recurring items. Each agency is then notified of its allocated amount or "slice of the pie" of the State's anticipated revenue. The agencies then plan their budget requests within the allocation and separately identify any amount requested above the allocation.

Agencies submit their budget requests to the Board's Budget Development Office for compilation and presentation to the Board. The Budget Development Office uses a standardized checklist to ensure that the agencies' requests will fit into a computerized format. The Office also checks to see that the requests match the funding allocations, fringe benefits are accurately computed, correct computer codes are assigned to object classes and subsidiary financial sheets balance to

summary financial sheets. Once the requests are compiled, the Board holds public hearings at which agencies give presentations. After the hearings are concluded the Board's budget is presented to the General Assembly.

After the annual Appropriation Bill is enacted by the Legislature, it is the duty of the Comptroller General to see that agencies do not expend more than has been appropriated to a particular line item. Additionally, a requirement is contained in Section 129 of the 1979-80 Appropriation Act which requires agencies to plan their budget expenditures based on a quarterly allotment of funds.

In order to assess the degree to which agencies are justifying their budget requests, this review focuses on three major aspects of the budget cycle...preparation, execution and control. Proper design and management of these aspects of the budget process enhances the State Budget and Control Board's ability to assure the justification of all agency expenditures.

The Council found that four components of the State's system need to be improved; more detailed budget analysis is needed, budget hearings can be conducted to focus more specifically on agency justification, better control and justification of agency transfers can be achieved, and quarterly monitoring of agency expenditures will allow closer oversight. These weaknesses in the budget process are discussed in the following paragraphs.

Need for Detailed Budget Analysis

The Budget Development Office does not perform detailed analysis or prepare alternative proposals to agency budget requests. When

agencies submit annual budget requests to the Budget and Control Board, the Budget Development Office does not investigate these requests to determine if agencies are fully justifying recurring expenses or properly supporting requests for additional funding as required by law. Section I-A of the 1978-79 Appropriation Act states that the Budget and Control Board will require each State agency to justify the "entire amount of money it is requesting." The Act further states, "It is the intent of this section that each State agency, department or institution shall be required to justify its recurring expenses, as well as any new or additional expenses."

There appear to be four major reasons why the State's budget is formulated without in-depth review and analysis. First, the State's system of allocating each agency a "slice of the pie" of the Board's preliminary revenue estimate is not conducive to analyzing agency budget requests, especially recurring expenses. A pattern has evolved whereby State agencies are not clearly required to justify their use of this allocation except for the amount by which their budget requests exceed the allocation level. Second, the Board is not providing clear guidelines to ensure that its budget staff performs critical analysis of agencies' budget requests. Alternative proposals for requests for improvements are not formulated for the Board. In addition, control of expenditures by the Board has not ensured that agencies are spending strictly in accordance with the intent of the Appropriation Act. For example, funds requested and appropriated, based on the justification of replacing needed kitchen equipment in an institution, should not be used to purchase office equipment. Such in-depth monitoring can be done if periodic reporting and analysis is made throughout the year.

The Budget Development Office needs to set standards and develop procedures to perform in-depth budget analysis. No steps have been taken to ascertain what documents and related information are available to aid analysis, which documents would be most useful for analysis, and that State Budget Analysts are trained to use them. Presently detailed analysis is done only upon request and is usually limited to single items in the budget.

Finally, during the period when agency budget requests are submitted, the Budget Development Office spends most of its time proof-reading the requests so that a budget document can be produced. The analysts receive the budget requests and go through a standardized check list to ensure that the requests will fit into a computerized format. The analysts also check to ensure that the requests match the funding allocations, fringe benefits are accurately computed, correct computer codes are assigned to object classes, and subsidiary financial sheets agree with summary financial sheets. Analysts also correct spelling, verbiage and punctuation on budget requests. This practice does not maximize the use of the six high level State Budget Analysts (Pay Grade 40: Average Salary: \$24,050).

Analysis and alternative proposals are methods to check the continued funding of nonessential or duplicate programs. These methods also serve to halt or slow the continued growth in agency budgets where programs continue to expand through increased funding without full justification.

Without in-depth budget analysis and the consideration of alternative proposals, the Budget and Control Board cannot fully assure that

agency budget requests represent actual budgetary needs. Such analysis would assure that the Board has adequate information to determine whether an agency's budget is the best allocation of the State's resources for programs.

The current system of preparing the Board's budget does not allow for detailed review of ongoing operations and expenditures of State agencies. There is little effort to determine which State agencies' programs are obsolete or which programs are providing only marginal benefits. Without close scrutiny, resources going to obsolete or marginal programs can neither be reduced nor diverted to programs yielding greater benefits. Money released by the discovery of obsolete programs could be used to decrease the total need for funds requested by an agency, to expand a higher priority program or to reduce taxes.

In conclusion, analysis could be improved by concentrating on two major areas, the "current level budget" and the "improvement request." The "current level budget" is the amount of money an agency needs to continue its current level of services. Current level budgets are examined by comparing the request with the current year's appropriations and last year's expenditures. Increases and decreases for items should be analyzed at the most detailed budget level. Detailed schedules should be established for certain expenditure items, such as travel, in order that funds requested for these items can be closely examined and justified. These schedules would also identify which items in a budget request are recurring expenses and which are non-recurring items.

Agency requests for "improvements" should be fully justified before they are approved. This area of analysis requires the budget

analyst to examine requests to determine not only the appropriateness of the need but whether the amount requested for the new item is justified. The analyst should also determine if the program needs to be funded in the current year, asking what would happen if it is not funded, and can the program be accomplished through other means. This is the area where the Board must set clear goals and objectives and guidance in what programs should be funded in the State's budget.

RECOMMENDATIONS

THE BUDGET AND CONTROL BOARD SHOULD ENSURE THAT IN-DEPTH BUDGET ANALYSIS OF AGENCY BUDGET REQUESTS IS PERFORMED IN ACCORDANCE WITH LAW. THE RECENT APPOINTMENT OF A DEPUTY STATE AUDITOR OVER STATE PLANNING, BUDGET DEVELOPMENT, AND THE GRANTS REVIEW UNIT SHOULD AFFORD A TIMELY OPPORTUNITY FOR ESTABLISHING THE POLICIES AND PROCEDURES TO CARRY OUT MORE THOROUGH AND BETTER COORDINATED REVIEW OF BUDGET REQUESTS AND THEIR JUSTIFICATION.

THE BUDGET DEVELOPMENT OFFICE SHOULD DEVELOP POLICIES AND PROCEDURES DIRECTING SENIOR BUDGET ANALYSTS TO PERFORM BUDGET ANALYSIS AND PREPARE ALTERNATIVE PROPOSALS TO AGENCY BUDGET REQUESTS.

THE CLERICAL DUTIES NOW PERFORMED BY THE SIX STATE BUDGET ANALYSTS (GRADE 40) SHOULD BE ASSIGNED TO THE BUDGET ANALYSTS AND ASSISTANTS WITH LOWER PAY GRADES. THE SIX SENIOR BUDGET ANALYSTS SHOULD BE ASSIGNED THE RESPONSIBILITIES OF REVIEWING, EVALUATING, ANALYZING AND PREPARING ALTERNATIVE PROPOSALS TO AGENCY BUDGET REQUESTS. THE BUDGET DEVELOPMENT OFFICE SHOULD USE THE BUDGET ANALYST POSITIONS AS A TRAINING GROUND FOR FUTURE SENIOR BUDGET ANALYSTS.

Budget Hearings Do Not Focus on Justifying Requests

State agencies do little justifying of their budget requests when they appear at the Budget and Control Board's budget hearings. The 1978-79 Appropriation Act, Section 1A directs the Board to require each State agency to justify the entire amount of money it is requesting.

The State Budget and Control Board shall, prior to making its annual recommendations to the General Assembly of the amounts to be appropriated to the various State agencies, departments and institutions as required by Section 2-7-60 of the 1976 Code, require each such agency, department or institution to justify the entire amount of money it is requesting. It is the intent of this section that each State agency, department or institution shall be required to justify its recurring expenses as well as any new or additional expenses. [Emphasis Added]

The formal budget hearing is one of the mechanisms available to the Board to have agencies justify their requests. Such hearings should concentrate on gathering evidence and taking testimony to justify the need for and use of public funds. The current budget

hearing procedure strays from this purpose especially where justification of recurring expenses is concerned.

Audit Council staff attended 42 of a scheduled 55 agency budget request hearings held by the Board during September and October 1979. When the hearings were convened, the Board and any attending legislative members were given a package which contained detailed budget requests primarily for funds above the agencies' allocations. These were apparently to be studied during the course of the hearing. The members were not provided with a simplified breakdown of the requests, any alternative proposals formulated by the Board's budget analysts or any reports on the agencies such as State Auditor's reports.

The hearings did not focus on the actual budgetary needs of State agencies. There was very little questioning on the use of agencies' allocations or the need for recurring expenses in their budgets. The few budgetary questions asked tended to focus only on an agency's request for new programs. Agencies were allowed to present slide shows, show off fossils, demonstrate museum relics and spend time which did not focus on justifying the need for their monetary requests.

Because of the way hearings are conducted they do not produce a critical review of agencies' budget requests and the Board members have to rely mostly on the agencies to supply them with information. Without independent information the Board cannot fully assess budget requests and propose alternatives. As a result the Board must spend time probing agencies for information and the time available for justification is not maximized. Since last year's new programs become this year's funding allocation, and no one is fully measuring or questioning the effectiveness of those new programs, the State's budget continues to grow incrementally.

RECOMMENDATIONS

THE BUDGET AND CONTROL BOARD'S BUDGET HEARINGS SHOULD BE SCHEDULED TO ALLOW SUFFICIENT TIME FOR:

- (1) DETAILED ANALYSIS OF AGENCIES' BUDGET REQUESTS, THE FORMULATION OF ALTERNATIVE PROPOSALS, AND PREPARATION OF THE BOARD'S BUDGET RECOMMENDATIONS.
- (2) STAFF OF THE STATE AUDITOR SHOULD MEET WITH THE BOARD TO DISCUSS ANALYSIS AND PROPOSALS SO THAT THE BOARD CAN MAKE RECOMMENDATIONS BASED ON FULLY JUSTIFIED NEEDS.
- (3) AGENCIES SHOULD BE NOTIFIED OF THE BOARD'S RECOMMENDATIONS AND THE DATES SCHEDULED FOR BUDGET HEARINGS.
 - (a) IF AN AGENCY AGREES TO THE BOARD'S RECOMMENDATIONS, THERE WOULD BE NO NEED FOR A HEARING.
 - (b) AGENCIES REQUIRING BUDGET HEARINGS SHOULD BE SCHEDULED TO ALLOW MORE TIME FOR THE LARGER AGENCIES AND THE MAJOR FUNDING DECISIONS.

(4) A SIMPLIFIED FORM SHOULD BE DEVELOPED TO PRESENT AGENCY BUDGET REQUESTS TO THE BOARD. THE FORM SHOULD INCLUDE THE PREVIOUS YEAR'S ACTUAL EXPENDITURES, CURRENT BUDGET, AGENCY REQUEST AND THE BUDGET OFFICE'S RECOMMENDATIONS. THE BUDGET OFFICE'S RECOMMENDATIONS SHOULD INCORPORATE INFORMATION FROM THE STATE PLANNING OFFICE AND THE GRANTS AND CONTRACTS REVIEW UNIT. SOURCES OF REVENUE AND OTHER ITEMS DEEMED APPROPRIATE SHOULD ALSO BE INCLUDED IN THE FORM. A SUMMARY OF ANY PERTINENT REPORTS, SUCH AS STATE AUDITOR'S REPORTS, SHOULD BE ATTACHED TO THE FORM. ONCE DEVELOPED, THIS FORM SHOULD REPLACE THE NEED FOR REPRODUCING COPIES OF EACH AGENCY'S DETAILED BUDGET REQUEST FOR PRESENTATION TO THE BOARD.

AFTER THE BUDGET OFFICE HAS PREPARED THE STATE'S BUDGET AND DISCUSSED IT WITH THE BOARD, BUDGET MEETINGS, OPEN TO THE PUBLIC, SHOULD BE HELD FOR REVIEWING AGENCY BUDGET REQUESTS. HOWEVER, PARTICIPATION SHOULD BE LIMITED TO THE BOARD, ITS BUDGET STAFF,

AGENCY DIRECTORS AND THEIR BUDGET STAFFS.
THE MEETINGS SHOULD CONCENTRATE ON AGENCIES
JUSTIFYING THEIR BUDGET REQUESTS TO INCLUDE
RECURRING EXPENSES.

Transfer System Needs Improvement

Introduction

When the General Appropriations Bill is enacted by the Legislature, each agency's appropriated accounts are set up on the books of the Comptroller General. It is the duty of the Comptroller General to see that an agency does not expend more than has been appropriated to a particular account. The agency is to expend its funds throughout the year in accordance with its appropriations.

In actuality, money is transferred between accounts as the need arises using a transfer request Form 300. The agency initiates the transaction by submitting four copies of the form to the Budget Development Office. The Budget Analyst assigned to the agency reviews the request, and the final decision is made by the Director of the Budget Development Office. This procedure was implemented in October 1979. Prior to that time, final approval rested with the Business Manager of the State Auditor's Office.

When the request is approved, one copy is filed in the Budget Development Office, one goes to the Comptroller General for posting, one goes to the Treasurer and one is returned to the agency.

Control of Transfers

The Legislative Audit Council has found that greater control is needed in South Carolina for the movement of funds over the course of the budget year. At LAC's request, the Comptroller General's Office provided information on transfer activity. The dollar volume of intra-departmental transfers (transfers within agencies) for FY 78-79 for State funds was \$79,247,000. Total transfer activity (within and between agencies and including all State, Federal and other funds) for FY 78-79 was \$565,336,000. There were 3,917 transfer forms processed for the total transfer activity during the year.

These transfers do not necessarily represent changes in the way the Legislature appropriated money for FY 78-79 since certain bookkeeping items also go into the records as transfers. The Legislative Audit Council has Fiscal Accountability Act reports that detail transfers by account number, but statewide aggregate figures are distorted by inconsistent lump-sum reporting. In short, it would be very difficult to arrive at a dollar total for transfers which alter the way the Legislature intended funds to be appropriated, without manually analyzing each agency's accounts. No one at the State level is currently doing any such analysis of transfer activity to compare the amounts appropriated to the actual use of funds by line item.

The Budget Development Office estimates that 99% of all transfer requests submitted are approved. An Analyst can recommend denying a transfer request but rarely does so, and the Director of the Budget Development Office has the authority to override that denial. Further, no record of denied requests is maintained by the Budget Development

Office since all copies of the disapproved Form 300 are returned to the agencies.

Form 300 is a debit and credit document without cumulative information or account balances. The revised Appropriation Transfer form to be used when the first stages of the new State Accounting and Reporting System (STARS) is implemented for the 1981-82 budget cycle is also a debit and credit document without cumulative information or account balances. If the Analyst wishes to review a transfer transaction, he may consult a cumbersome "Statement of Activity" which is available on request from Data Processing. The "Statement of Activity" shows original appropriations, receipts, and disbursements for each account. Transfers are shown cumulatively, without account numbers. The Business Manager receives a report from which transfer activity may be extracted by account number, but no transfer analysis is specifically generated by the computer.

Furthermore, there is no budget amendment process whereby an agency's current budget as amended by transfers can be easily identified. Such a process would make a distinction between routine transfers and those that alter legislative intent. Any change of "intent" would be brought to a policy-making board for approval as a budget amendment. The STARS mini-coding capability would allow the separate identification of the various types of transfers.

Budget Analysts are not provided with standard procedures or guidelines for analyzing transfers. When LAC interviewed the Analysts in August and September, some were unaware of the availability of a "Statement of Activity."

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The only transfer instructions the agencies receive are found on the request form itself as follows: "This form should be accompanied with a letter indicating fully the necessity of the transfer being requested. No commitment should be made in anticipation of the approval of a transfer."

LAC examined a sample of approved transfer requests for 1978-79 on file in the Budget Development Office, and found some transfer requests had no accompanying justification at all, some had nominal justification and some appeared to have sufficient justification. Nominal justifications included statements such as "to cover necessary expenditures," "exceeded estimated needs," and "we were under-appropriated." One justification stated, "Your immediate approval of this transfer is requested inasmuch as we are submitting a voucher today to the Comptroller General." This is in clear violation of the stipulation that no commitment be made in anticipation of the approval of a transfer. Recently after this file was reviewed by LAC, a memo was sent to all State agencies which stated, among other things that "all transfer requests should be accompanied by a letter of explanation detailing the necessity of the request."

The Legislative Audit Council reviewed the system for control of transfers in Georgia and North Carolina. Of interest in the North Carolina system is the procedure whereby the agencies submit monthly budget amendment reports detailing monthly, quarterly and year-to-date expenditures, rate of expenditure, unexpended balance and encumbrances. The Analyst's chief criterion in analyzing transfers is legislative intent and to that end he attends most meetings of Appropriations Committees.

In Georgia, all agency requests for transferring funds between object classes are brought before a Fiscal Affairs Subcommittee of the House and Senate. The Committee is convened by the Governor when he feels there are sufficient requests to justify a meeting, usually quarterly. Agencies are notified that in presenting their requests, they should be prepared to lapse any funds identified for transfer in the event the transfer is not recommended. Their transfer request form requires the following information: 1) Nature of the transfer; 2) Reason that the transfer need was not ascertained at the time the current budget was prepared; 3) Detail of proposed expenditures; and 4) Estimated lapse of State surplus funds by object on June 30 (before transfer).

South Carolina's laws clearly indicate the Legislature's intent that there be strict control over the transferring of appropriations. Section 11-9-20 of the 1976 South Carolina Code states:

It shall be unlawful for any officer, clerk or other person charged with disbursements of State funds appropriated by the General Assembly to exceed the amounts and purposes stated in such appropriations, or to change or shift appropriations from one item to another; provided, that transfers may be authorized by the General Assembly in the annual appropriation act for the State. [Emphasis Added]

Section 141 of the 1978-79 General Appropriations Act and Section 140 of the 1979-80 Act state:

...transfers of appropriations herein provided may be made within departments, upon the unanimous approval of the State Budget and Control Board. [Emphasis Added]

Budget procedures have evolved over time into a system where there are minimal guidelines for the Analysts or the agencies, complete justifications are not required, transfer analysis reports are not provided

to the Budget Analysts, no records are kept of disallowed transfer requests and there is no budget amendment process. Although the Appropriation Act says "by unanimous approval of the State Budget and Control Board," only transfers necessitating movement in or out of Personal Services are brought before the Board. No reports of cumulative transfer activity are made to the Board, indeed, transfer activity measured by number of requests alone is too monumental to be brought before the Board.

Ineffective control of transfer activity could allow legislative intent to be undermined if the funds transferred are not closely scrutinized. Improvements are needed in the control of transfers which would ensure adequate legislative oversight.

RECOMMENDATIONS

A BUDGET AMENDMENT PROCESS SHOULD BE INSTITUTED WHEREBY BEFORE AN AGENCY TRANSFERS FUNDS IT HAS RECEIVED PRIOR APPROVAL FROM THE BOARD. AFTER BOARD APPROVAL EACH AGENCY SHOULD SUBMIT AN AMENDED BUDGET (SPENDING PLAN) TO THE BUDGET DEVELOPMENT OFFICE.

THE STATE BUDGET AND CONTROL BOARD SHOULD MEET QUARTERLY FOR THE EXPRESS PURPOSE OF HEARING AGENCY REQUESTS FOR THE TRANSFER OF FUNDS. AGENCIES SHOULD BE NOTIFIED TO BE PREPARED TO LAPSE THE FUNDS IF THE TRANSFER IS NOT APPROVED.

GUIDELINES SHOULD BE DEVELOPED FOR ANALYZING TRANSFERS TO ENSURE THAT EACH ONE IS A CRITICAL NEED.

A. THE FOLLOWING TYPE OF QUESTIONS SHOULD BE ANSWERED:

1. CAN THE MATTER WAIT FOR LEGISLATIVE ACTION WHEN THE SUPPLEMENTAL BUDGET IS UNDER CONSIDERATION?
2. DID THE AGENCY INITIALLY REQUEST ENOUGH MONEY FOR THE ACCOUNT? WHY NOT?
3. WHY ARE THERE EXCESS FUNDS IN THE ACCOUNT TO BE TRANSFERRED OUT?

B. DIFFERENT LEVELS OF TRANSFER ACTIVITY SHOULD BE IDENTIFIED AND TREATED APPROPRIATELY:

1. ROUTINE TRANSFERS, SUCH AS LOANS AND REPAYMENTS AMONG ACCOUNTS, SHOULD BE ACCOUNTED FOR SEPARATELY. THESE SHOULD NOT NECESSARILY REQUIRE BOARD APPROVAL. SUCH

TRANSFERS COULD BE APPROVED BY
THE COMPTROLLER-GENERAL'S OFFICE.

2. TRANSFERS BETWEEN OBJECT CLASSES
AND BETWEEN PROGRAMS SHOULD
REQUIRE CLOSE ANALYSIS, A RECOMMEN-
DATION BY THE AUDITOR'S OFFICE AND
APPROVAL BY THE BOARD. SUCH
TRANSFERS SHOULD REQUIRE A BUDGET
AMENDMENT TO ACCURATELY REFLECT
EACH AGENCY'S SPENDING PLAN.
 3. THE PRACTICE OF REQUIRING BOARD
APPROVAL FOR TRANSFERS AFFECTING
PERSONAL SERVICE SHOULD BE
CONTINUED.
- C. THE TRANSFER FORM SHOULD SHOW SPECIF-
ICALLY WHAT IS TO BE INCLUDED AS
JUSTIFICATION.
- D. A RECORD OF DISALLOWED TRANSFERS
SHOULD BE MAINTAINED FOR USE IN
ANALYZING THE FOLLOWING YEAR'S BUDGET
REQUEST.

Need for a Budget Amendment Process

In an earlier study the Audit Council found that Federal funds for 1975-76 were understated by 7% of the total recommended budget for that year. This meant the agencies had 7% more to expend than was envisioned in the Budget and Control Board recommendation. A current review of the budget documents for FY 77-78 reveals that the underestimation for that year is again 7% of the total recommended by the Budget and Control Board. In the earlier study the Audit Council recommended a legislative authorization procedure be instituted to bring these funds under legislative control, and a budget amendment process be instituted to provide a clear trail from the budget as originally authorized to the budget as actually expended.

These Federal funds have been brought under legislative authority by virtue of the establishment of the JARC. However, at this time, no budget amendment process has been instituted. Once an agency receives approval for a proposal, it is up to the agency to report to the GCRU the outcome of its grant application. The GCRU is dependent on these agency reports for information as to whether the application was approved or rejected, and if approved, the level of funding actually received. An agency does not have to show Budget and Control Board approval prior to having new Federal funds added to its accounts. The General Appropriation Bill for FY 78-79, in the version approved by the House, contained a proviso whereby agencies spending Federal funds without Budget and Control Board approval would have their general budget automatically reduced by the amount of the unapproved Federal funds received. However, this proviso was deleted from the Bill. A review of agency logs on file in the GCRU showed the reporting of Federal

funds received by agencies to be spotty at best. Therefore, it is not possible at any point in time to look at centralized records and determine the agencies' current authorized expenditure level.

As part of the STARS procedure, the agencies will not be able to set up accounts for their Federal funds without reporting the actual level of such funding to the GCRU. This reporting, if put in the form of Budget amendments, should increase accountability for and control over Federal funds statewide. However, it is not yet known when this system will be implemented.

RECOMMENDATIONS

A BUDGET AMENDMENT PROCESS SHOULD BE INSTITUTED FOR AGENCIES WISHING TO SPEND FEDERAL OR OTHER FUNDS ABOVE THE LEVEL AUTHORIZED IN THE APPROPRIATION ACT. AGENCIES SHOULD SUBMIT AMENDED BUDGET PLANS TO THE BOARD AND JARC FOR APPROVAL. A QUARTERLY MEETING OF THE STATE BUDGET AND CONTROL BOARD AND THE JARC SHOULD BE HELD FOR THE EXPRESS PURPOSE OF CONSIDERING SUCH BUDGET AMENDMENTS. ONLY UPON THEIR APPROVAL SHOULD AN ACCOUNT BE SET UP FOR THESE FUNDS ON THE BOOKS OF THE COMPTROLLER GENERAL, OR AN EXISTING ACCOUNT ADJUSTED.

CHAPTER III

RELATED BUDGET ISSUES

Introduction

The budget process is the mechanism through which State Government is expected to achieve accountability over its expenditure of funds. As such, it is important that all aspects of the process be thoroughly reviewed to ensure that the General Assembly can direct the State's resources to the changing needs of the public and know what results are achieved. This chapter will provide a brief overview of some areas related to the budget process which may require further legislative attention.

Statewide Accounting and Reporting System

The major objective of the Statewide Accounting and Reporting System (STARS) is to provide for the centralized accounting and reporting of financial data in accordance with the program budget structure. The STARS data bank is expected to eventually free the Budget Analysts from voluminous data editing and free the agencies from having to regenerate historical data each year. The classification structure is expected to provide consistency throughout the budget, accounting, and financial reports of the State. It is also expected to facilitate program budgeting through the use of program codes encompassing statewide functions which cross agency lines. Through the use of revenue object coding and a mandatory approval system prior to setting up revenue accounts, control over non-General Fund expenditures is

expected to be tightened. STARS will be the basic means for retrieving and arranging much budget information.

RECOMMENDATION

THE IMPLEMENTATION, OPERATION AND USE OF
STARS SHOULD BE CONSIDERED FOR FUTURE
IN-DEPTH REVIEW.

Bonding for Capital Improvement Projects

State agencies' bonding requests are authorized through the enactment of a bond act separate from the State's annual Appropriation Act. Therefore, when the State's budget is formulated the General Assembly is acting without information which would inform them of the increased costs that projects funded through a bond act will add to the State's annual operating budget. In addition, some State agencies have been allowed to use bond acts to fund items which could be financed from General Revenue funds.

General Obligation Bonds are long-term debts, 10 to 30 years, incurred by the State. They represent an "IOU" or pledge by the State to repay the bond buyer the amount of the bonds by a specified date, plus a fixed annual rate of interest on the bond's value. The purpose of incurring this debt is to distribute the cost of a bond-financed project over the lifetime of that project. In this way future beneficiaries of a project also share in its cost.

The principle advantage of this long-term debt financing is that it allows the State to undertake a capital improvement project which could not be financed from current revenues. It also spreads the payments

for a project over a period of 10 to 30 years so as not to place an undue burden on current revenues.

This method of financing capital improvement projects through long-term debt is not without perils. The General Obligation Bonds of a state are backed by the full faith and credit of that state's ability to generate revenue to meet its budget and pay the debts incurred by selling bonds. A state's bond rating is a measurement of that state's ability to meet these requirements. A bond rating also determines how easily a state can sell its bonds and what terms it can receive in the bond market. A reduction in a state's bond rating, as has occurred to Michigan and Connecticut over the past four years, can adversely affect a state's overall financial situation. Currently South Carolina has the highest bond rating possible, a triple A (or AAA).

Capital improvement needs are identified by individual State agencies with little central coordination devoted to capital improvement planning. Consequently, the State "backs into" capital improvement budgeting because it is only after a project has been completed that the State begins budgeting the operating costs and projecting its future costs of operation.

Without long-range capital planning the State cannot effectively evaluate alternatives to financing capital improvements. For example, projects funded through bond acts could be analyzed using preestablished guidelines or criteria to determine if they are:

- (1) Durable and have an extended useful life.
- (2) Not subject to inherent risk of failure or rapid technological obsolescence.
- (3) Not primarily designed to fulfill interim needs.

- (4) Nonrecurring and confer long-term benefits.
- (5) Representative of a permanent improvement which enriches the utility or dollar value of the State's equity in capital assets.

The Council reviewed State agencies' permanent improvement requests for 1979-80 and 1980-81 which were submitted to the Legislature. Using some of the above criteria, capital projects such as computers, equipment, airplanes and property purchases apparently would not meet the durability or obsolescence standards needed to justify long-term debt financing.

Currently the State has a total Capital Improvement Bond authorization of \$702,524,699.19 not including State Institution and Plant Improvement Bonds. With such a large authorization permanent improvement project debt, financing should be undertaken only when the resulting asset fulfills the needs and long-term goals and objectives of an agency. While the needs of an agency may be difficult to estimate, such estimation provides a foundation for effective capital planning and budgeting.

This would aid the State in determining precise permanent improvement needs of State agencies and the costs these projects will add to the annual operating budget. By knowing its overall needs the State can propose alternatives, such as consolidating capital asset requests, or explore other methods in order to reduce these capital improvement needs and their resulting operating costs.

RECOMMENDATIONS

THE GENERAL ASSEMBLY SHOULD COMMISSION A STUDY OF ITS BONDING PROCESS TO INCLUDE PLANNING, BUDGETING AND THE USE OF BOND FUNDS. THIS STUDY SHOULD INVESTIGATE THE

DEVELOPMENT OF CAPITAL BUDGETING AND ITS
INCLUSION IN THE STATE'S BUDGETARY PROCESS.

Printing of the Appropriation Bill

The printing of the Appropriation Bill at each step of the budgetary process is costly and consumes too much time. To print the bill at each step causes delays in the timely enactment of the State's Appropriation Act.

The House of Representatives Rule 5.3 requires that the Appropriation Bill be printed at each stage in the budgetary process. The rule states:

All State Appropriations Bill shall be printed at each stage in their passage, so as to show the amounts appropriated for any of the purposes therein for the fiscal year immediately preceding, the amounts requested by the institution or departments, the amounts recommended by the Budget Commission (sic), the amounts approved by the Ways and Means Committee, the amounts passed by the House, the amounts approved by the Senate Finance Committee, the amounts passed by the Senate, and the amounts agreed upon by the Free Conference Committee.

Time and money can be saved if the General Assembly would begin using a computer printout of the Appropriation Bill for its budget committee hearings and deliberations. Currently, it takes 5 to 13 days to receive a printed copy of the Appropriation Bill while a computer printout of the bill could be returned at least several days earlier. The Senate Finance Committee currently uses a computer printout of the bill when it conducts its budget hearings and deliberations and the State Budget Document is a copy of a computer printout.

Currently, the State sends the master printout to the printers who must then reset the type for each page of the bill in order to print it. According to information from the State's General Services Division, using a master computer printout to print the bill would reduce the cost of printing from the current \$19 per page to an average of \$3.50 per page. A significant savings could be realized since the cost of printing has risen from \$48,121.68 in 1975 to \$84,044.57 in 1979.

RECOMMENDATION

CONSIDERATION SHOULD BE GIVEN TO AMENDING HOUSE RULE 5.3 TO ALLOW THE USE OF A CERTIFIED COMPUTER PRINTOUT IN THE BUDGETARY PROCESS. THIS COMPUTER PRINTOUT COULD BE USED FOR COMMITTEE HEARINGS AND DELIBERATIONS, WHILE A MASTER COPY OF THE COMPUTER PRINTOUT COULD BE USED FOR PRINTING THE APPROPRIATION BILL.

APPENDICES

APPENDIX A

STATUTES AT LARGE LOCAL AND TEMPORARY LAWS—1978

(R794, H3678)

No. 651

A Joint Resolution To Provide For A Revised Structure And Content Of The General Appropriation Act So That, Beginning With The Fiscal Year 1978-79, All Funds Involved In The State Government Shall Be Subject To Formal Legislative Authorization; To Provide For A Revised Format For The Annual State Budget, Commencing With The Fiscal Year 1979-80, So As To Adequately Present Budgetary Data Which Clearly Defines The Programs Carried Out By The Various Agencies, Departments, Agents, And Commissions Of The State And That Such Program Definitions Should Contain Clear Descriptions Of Program Objectives, Program Cost, And Measurements Of Program Effectiveness; And To Continue The Joint Legislative Committee Created In Section 1B Of Part 1 Of Act 219 Of 1977 (The General Appropriation Act For 1977) And To Further Prescribe Its Duties And To Provide Certain Exceptions To Review And Approval By The Board And The Committee.

Be it enacted by the General Assembly of the State of South Carolina:

Findings

SECTION 1. The General Assembly finds that in Section 1B, Part 1 of Act 219 of 1977 (the State General Appropriation Act) it expressed its intent to modify the structure and content of the annual state general appropriation act so as to specifically authorize and control the expenditure of those funds involved in the operation of the state government over and beyond those appropriated out of the general fund, and that the modifications would become effective with the general appropriation act for 1978-79. It further finds that in Section 1B the General Assembly created a joint legislative committee to be responsible for determining required changes, not only in the general appropriation act but also in the format of the annual state budget.

Form of general appropriation act to be changed

SECTION 2. The General Assembly hereby reaffirms its intent, as expressed in Act 219 of 1977, to modify the structure and content of the state general appropriation act so as to subject to the legislative appropriating process all funds expended within the state government, including not only those derived from the general fund but those from the federal government and any other source and that the process shall be effective with the general appropriation act for 1978-79.

APPENDIX A (CONTINUED)

Joint Appropriations Review Committee

SECTION 3. The joint legislative committee created in Section 1B, Part I of Act 219 of 1977 is hereby established as a permanent committee to be known as the Joint Appropriations Review Committee with such powers and duties as may be provided for in this act.

State agencies not to receive or expend funds without approval

SECTION 4. While the General Assembly is in session, with the exception of appropriations from the General Fund and those provided for in Sections 7, 8 and 9 of this act, no agency or institution of state government shall expend any funds without prior approval of the State Budget and Control Board and the concurrence in such approval by the Joint Appropriations Review Committee. In determining their position with respect to any proposed receipt or expenditure, the Board and the Committee shall consider among other things the public benefit to be derived from the program or service, and the impact of the proposal on the future finances of state government.

Proposals shall originate with the agency or institution identified with the funds which shall submit them to the Board for its approval. The Board shall then furnish the requests and its recommendations to the Joint Appropriations Review Committee, which shall furnish to the Board within fourteen days a statement of concurrence or nonconcurrence as to the recommendations. If the Committee fails to act within the allotted time the action of the Budget and Control Board shall be deemed to be approved.

Provided, however, the provisions of this section shall not be construed to apply to funds generated at the local level from local appropriations whether or not such funds are used with state funds in the implementation of programs or the delivery of services in cooperation with or under the supervision of agencies of state government.

Further

SECTION 5. During periods the General Assembly is not in session, with the exception of appropriations from the general fund and those provided for in Sections 7, 8 and 9 of this resolution, no agency or institution of state government shall expend any funds without prior approval of the State Budget and Control Board. In determining its position with respect to any proposed expenditure, the Board shall consider among other things the public benefit to be derived from the program or service, and the impact of the proposal on the future finances of state government.

Proposals shall originate with the agency or institution identified with the funds which shall submit them to the Board for its approval. Prior to making its decision, the Board shall furnish the request to the Joint Appropriations Review Committee, which shall furnish to the Board within fourteen days any advice or recommendations which it deems appropriate. The Board shall give consideration to the advice and recommendations when making its final determination as to whether to approve or disapprove the request.

APPENDIX A (CONTINUED)

The Board shall use its discretion in the absence of advice or recommendations from the Committee. *Provided*, however, the provisions of this section shall not be construed to apply to funds generated at the local level from local appropriations whether or not such funds are used with state funds in the implementation of programs or the delivery of services in cooperation with or under the supervision of agencies of state government. The Board, in cooperation with the Committee, shall make such rules and procedures as may be necessary to carry out the purposes of this resolution.

Review of federal grant applications

SECTION 6. When reviewing federal grant applications the Board and the Committee shall determine the requirement or desirability for a single state agency designation. If the designation is found to be desirable or required the Board or Committee, with the concurrence of the Board or Committee in accordance, shall make the designation, with the procedures set forth in Sections 4 and 5.

When agencies may apply for research grants and student loans

SECTION 7. Notwithstanding the provisions of Sections 4 and 5 of this act, any state agency or institution may apply for and receive research grants and student loan funds from federal and private sources if the acceptance of the funds will not create a continuing obligation to commit state funds or state resources beyond the term of the grants. The grants may be applied for and received without prior review and approval by the Board or Committee but the receipt of the grants shall be reported to the Board and the Committee within fourteen days of notification of the award. Agencies and institutions receiving research grants shall not be required to remit indirect cost recoveries to the general fund.

Certain appropriations not to require approval

SECTION 8. Funds other than federal funds or those appropriated from the general fund, which are included in the state general appropriation act and authorized for expenditure, shall not require subsequent approval by the Board if the expenditures are in accord with the line item appropriation of the act.

When certain monies not to be returned to general fund

SECTION 9. The Board or Committee, in accordance with the procedure set forth in Sections 4 and 5, may waive the requirement that indirect cost recoveries or overhead cost reimbursements shall be returned to the general fund revenue if it determines it is in the best interests of the State and the agency or institution seeking the grants.

In making its determination, the Board or Committee shall make sure that the action shall not create within an agency or institution a fund of surplus money which can be used to expand programs without legislative approval.

APPENDIX A (CONTINUED)

What revised format to include

SECTION 10. The Board shall revise the structure of the annual state budget so as to present a format which clearly delineates each agency's and institution's programs, their sources of revenue, the associated program objectives, the total program costs and program effectiveness measurements.

In developing the revised budget format and procedures, the Board shall seek the advice and recommendations of the Committee in accordance with the procedure as set forth in Section 5.

Agencies to cooperate

SECTION 11. Notwithstanding any other laws, all agencies and institutions of the State shall cooperate fully with the Board and the Committee in the implementation of this act. Full cooperation shall specifically include, but not be limited to: (1) defining all programs carried out by a given state agency or institution, (2) submitting to the Board the state agency's or institution's 1979-80 budget in the format requested by the Board, and (3) reworking the state agency's or institution's 1978-79 budget so that the 1979-80 budget can reflect, in the format approved by the Committee and the Board, how fiscal year 1978-79 funds were expended.

Recommendations for additional legislation

SECTION 12. The Committee shall prepare and submit to the Ways and Means Committee of the House and the Finance Committee of the Senate a comprehensive recommendation regarding any further legislative action which may be needed to implement the intent of this resolution.

Duties of Legislative Audit Council

SECTION 13. The Legislative Audit Council shall conduct a review and evaluation of the revised budget process and procedures and report its conclusion to the Board and the Committee by January 8, 1980.

Time effective

SECTION 14. This act shall take effect upon approval by the Governor.

Approved the 23rd day of July, 1978.

APPENDIX B

APPROPRIATIONS FOR 1977-1978

STATE OF SOUTH CAROLINA

Part I, Operation of State Government

SECTION 1A

The State Budget and Control Board shall, prior to making its annual recommendations to the General Assembly of the amounts to be appropriated to the various State agencies, departments and institutions as required by Section 2-7-6 of the 1976 Code, require each such agency, department or institution to justify the entire amount of money it is requesting. It is the intent of this section that each State agency, department or institution shall be required to justify its recurring expenses as well as any new or additional expenses.